No.

IN THE

Supreme Court of the United States

OCTOBER TERM 1943

ANDREW JERGENS,
Petitioner,

against

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF

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Petitioner prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit entered in the above entitled cause on June 15, 1943.

Opinions Below

The opinion of the United States Board of Tax Appeals (R. 26) is an unreported Memorandum Opinion, Docket No. 107,163, entered on August 28, 1942. The opinion of the Circuit Court of Appeals (R. 71) is reported in 136 F. (2d) 497.

Jurisdiction

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, 43 Stat. 938 (28 U. S. C. A. 347). The judgment of the Circuit Court of Appeals was entered on June 15, 1943 (R. 79). Petition for Rehearing was denied on July 17, 1943 (R. 86).

Questions Presented

Can a person possessing an *unexercised* power to withdraw trust property or income therefrom be taxed on the income under Sec. 22(a) of Revenue Acts of 1936 and 1938, even though he never withdrew, assigned, realized or otherwise enjoyed the property or income, where there is no contention that the trust under which the power was granted is not a bona fide trust or that it was created for the purpose of tax avoidance? Or stated another way—

Can A, the grantor of a trust, after directing the trustee to distribute currently the income to himself and others, make B taxable on the entire trust income by giving B the right, upon 5 days' written notice to the Trustee, to withdraw a portion of the corpus or the income, even though B does not exercise the right and does not actually or constructively receive, assign, realize or otherwise enjoy the property or the income therefrom?

Statutes Involved

The statutes involved are Sections 22(a), 161 and 162 of the Revenue Acts of 1936 and 1938, which are set forth in the Appendix.

Statement

In the proceedings before the Board of Tax Appeals the parties filed a Stipulation of Facts, and no evidence other than the Stipulation was offered. The pertinent facts are as follows:

In 1934, petitioner's wife, Amy Branch Jergens, as settlor, entered into a trust agreement with The First National Bank of Cincinnati, Ohio, and Andrew Jergens (the petitioner herein) as Trustees. Pursuant to the terms thereof, the settlor transferred to the Trustees certain shares of the stock and two policies of life insurance insuring the life of the petitioner. The policies of insurance had been applied for by the settlor, and pursuant to her request were issued on the ownership form, designating her as beneficiary, absolute owner of the policies and as the person obligated to pay all premiums (R. 46).

The trust agreement required the Trustees to collect the income from the stock, pay the expenses of the trust, and to apply the net income as follows: First, to pay the premiums on the insurance policies held by the Trustees; second, to pay $125.00 per month to one Lida Brady, an aunt of the settlor, together with $100.00 on Christmas and $100.00 on her birthday; and third, to pay the remaining net income in quarterly installments to the grantor so long as she should live (R. 50).

The trust agreement gave petitioner as an individual the right, on five days' prior written notice to the corporate Trustee, to withdraw any part of the corpus of the trust except the insurance policies, which he could withdraw only with the consent of the settlor. The trust further provided that petitioner had the power to alter, modify and/or amend the trust agreement in any respect, except that he could not make the proceeds of the insurance policies payable to his estate (R. 55).

The agreement provided that the trust should terminate on the death of the settlor, at which time the trust property should be distributed to the petitioner, if he was living at that time, otherwise to the issue of the settlor and the petitioner, or to their adopted children, and if none of these persons were living at the time of distribution,

then the trust property was to be held for certain charitable purposes (R. 56).

In the event that the petitioner predeceased the settlor, the corporate Trustee was to collect the proceeds of the insurance policies and hold same in trust and pay the income from the trust corpus to the settlor for life (R. 50).

During the taxable years the Trustees received dividend income from the stock and after paying the trust expenses, applied a portion of such income on the insurance premiums, distributed $1,700.00 each year to Lida Brady, and the remainder if any to the grantor (R. 47).

For the taxable years 1936, 1937 and 1938, the trust filed fiduciary income tax returns for the trust and reported as taxable income the amounts used by it to pay the insurance premiums. It claimed deductions for the amounts currently distributed to Lida Brady and the settlor (R. 48).

For the years 1937 and 1938 the settlor filed income tax returns and reported as taxable income the amounts distributed to her from the trust and paid income tax thereon. She did not receive any distribution from the trust in 1936 (R. 48).

In his deficiency letter for 1936, 1937 and 1938, the Commissioner determined that the entire net income of the Amy Branch Jergens' trust constituted taxable income to petitioner under Section 22(a) of the Revenue Acts of 1936 and 1938. The Board of Tax Appeals sustained the Commissioner's determination (R. 13 and 26).

Decision of the Circuit Court

The Circuit Court of Appeals, by a majority of two to one, affirmed the decision of the Board of Tax Appeals, citing a number of cases involving *donors* and *grantors* of trusts, and involving trust situations where the *grantors* had *retained* control over the trust corpus and income and had *realized* the *benefit* thereof by *directing* that the *income*

be paid over to *another person.* Whereupon the petitioner filed a Petition for Rehearing, pointing out that the instant case was distinguishable from those cases in that here the taxpayer was only the donee of an unexercised power, and was not the *grantor* of the trust and had not *realized* or *enjoyed* the income in any way whatsoever. That Petition for Rehearing was denied on July 17, 1943 (R. 86).

Specification of Error to Be Urged

The Circuit Court of Appeals erred in holding that, by reason of petitioner's unexercised power to withdraw a portion of the corpus and the income of a trust *created by another person,* he was taxable upon the entire income of the trust under Section 22(a) of the Revenue Acts of 1936 and 1938, even though petitioner did not receive, assign, realize, or otherwise enjoy any part of the corpus or income, and even though the income was distributed currently pursuant to *grantor's* directions and largely for *her benefit.*

Reasons for Granting the Petition

1. The decision of the Circuit Court involves "an important question of Federal law which has not been, but should be, settled by this Court.*

2. The Circuit Court has decided a Federal question in a way probably in conflict with applicable decisions of this Court, and its decision is not supported by the Supreme Court cases relied upon.*

3. The decision of the Circuit Court conflicts with the decision of the Circuit Court of Appeals for the Ninth Circuit in *Commissioner* v. *Giannini,* 129 F. (2d) 638, and also the decision of the Sixth Circuit in *Commissioner* v. *Mott,* 85 F. (2d) 315.*

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* Supreme Court Rule No. XXXVIII-5(b).

4. The decision of the Circuit Court raises "uncertainties in this area of Federal tax law," *Interstate Transit Lines* v. *Commissioner* (United States Supreme Court, No. 552, decided June 14, 1943), will result in administrative confusion, and will open a tax avoidance loophole not heretofore available to persons in high surtax brackets.

The reasons stated above will be discussed in the brief.

THE BRIEF

The Facts

The facts have been stated in the petition and will not be repeated here. However, taxpayer desires to emphasize the fact that during the taxable years the income was distributed currently pursuant to the directions given by the *grantor* (Amy Branch Jergens). She directed the Trustees:

(1) To pay the premiums on the insurance policies held in the trust (upon death of petitioner the corporate Trustee was to collect the insurance proceeds, hold in trust, and pay income to *grantor* for life); (2) to pay $1,700.00 per year to her Aunt Lida Brady; and (3) to pay the remainder of the income to the *grantor*. (Substantial sums were paid to *grantor* in 1937 and 1938.) The petitioner never received, assigned, realized or otherwise enjoyed any part of the income in any way whatsoever.

ARGUMENT

I

THE DECISION OF THE CIRCUIT COURT INVOLVES "AN IMPORTANT QUESTION OF FEDERAL LAW WHICH HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT"

The Circuit Court of Appeals has decided that Federal income tax should be assessed against petitioner even though he did not own the properties producing the income, and even though he did not actually or constructively receive, assign, realize, or otherwise enjoy the income therefrom in any way whatsoever. It is believed that this is the first instance where a Federal Court has held that a *bare unexercised right* to receive property or the income therefrom warrants the imposition of the tax. Surely this Court has never so held. Heretofore the courts have required not only control or dominion over the income, but also some measure of "realization" or "enjoyment" thereof. For instance, there is a line of cases where this Court has held donors or grantors of trusts taxable on income which they did not actually receive but in each of those cases the taxpayers *realized* the *benefit* of the income by *directing* that it be paid to their nominees. This is the line of cases relied on by the Circuit Court, but here the trust income was distributed currently in accordance with the directions of the *grantor, not the petitioner, and he did not actually or constructively receive any part thereof, nor did he realize or enjoy it in any way.* Here the petitioner was the mere donee of an unexercised power. This new concept of income is not only in conflict with principles laid down by other Circuit Courts, but it actually broadens the very concept of income as laid down by this Court. In fact, the decision results in an overlapping of income, that is, several persons are taxed on the identical income, and its general application will result in adminis-

trative confusion, inequities, and multiple litigation. This question is so fundamental and so important that it should definitely and promptly be settled by this Honorable Court.

II

THE CIRCUIT COURT HAS DECIDED A FEDERAL QUESTION IN A WAY PROBABLY IN CONFLICT WITH APPLICABLE DECISIONS OF THIS COURT, AND ITS DECISION IS NOT SUPPORTED BY THE SUPREME COURT CASES RELIED UPON

After stating the facts, the Circuit Court disposed of the legal question presented in one short paragraph. The real basis of its decision is stated in one sentence. It reads as follows:

> "It is the long-settled course of tax jurisprudence that such control over income warrants the imposition of the tax incidence of that income upon the person who commands its disposition whether he takes it for himself or not. *Reinecke* v. *Northern Trust Co.,* 278 U. S. 339; *Corliss* v. *Bowers,* 281 U. S. 376; *Lucas* v. *Earl,* 281 U. S. 111; *Helvering* v. *Clifford,* 309 U. S. 331; *Helvering* v. *Horst,* 311 U. S. 112; *Harrison* v. *Schaffner,* 213 U. S. 579."

Following the proposition that "control over income warrants the imposition of the tax," the Circuit Court has held that in the instant case petitioner is taxable on the trust income, despite the fact that he did not earn, receive, give, assign, transfer, realize or otherwise enjoy the benefits thereof in any way whatsoever.

Petitioner proposes to show that the cases cited and relied upon by the Circuit Court do not support any such proposition. Moreover, a study of those cases will show that the proposition stated by the Circuit Court is probably in conflict with the principle enunciated by the Supreme Court in those same cases.

The *Reinecke* case involved a *grantor* of two *revocable* trusts, and this Court held that the trust properties were includable in his estate for Federal Estate tax purposes. It is not apparent why the Circuit Court cited an estate tax case, but perhaps for the purpose of showing that there should be integration between the income and estate tax laws, that is, if the property would be includable in the taxpayer's gross estate, then he should be taxable on the income therefrom. But the instant case does not involve a *grantor* of a *revocable* trust, so the analogy does not follow. Taxpayer will show in a subsequent section of this brief that under a recent court decision, acquiesced in by the Commissioner, the trust properties here involved would not be includable in his estate for Federal Estate tax purposes. Therefore, if any analogy is to be drawn with estate tax cases, it would seem to follow that petitioner is not taxable on the income from properties which would not be includable in his estate. Surely the *Reinecke* case has nothing to do with the proposition for which it was cited.

Corliss v. *Bowers, supra,* involved a *grantor* of a *revocable* trust, taxable under Section 219(g) of the 1924 Act (Section 166 I. R. C.). Section 22(a) was not involved. There the *grantor* not only *reserved* the right to revoke, but he *directed* that the income be paid to his wife, thereby *actually exercising* his *command* over the income and thus *realizing* the *benefit* thereof. This case does not stand for the proposition that "control" alone warrants the imposition of the tax. It stands for the proposition that "control" plus the *exercise* of that *control,* warrants the imposition of the tax. There the taxpayer *realized* the *benefit* of the income by *directing* that it be paid to his wife. In that case this Court said:

> "But taxation is not so much concerned with the refinements of title as it is with actual command over

> the property taxed—*the actual benefit for which the tax is paid. If a man directed his bank to pay over income as received to a servant or friend, until further orders, no one would doubt that he could be taxed upon the amounts so paid.*" (Italics ours.)

Thus this Court made it plain that the tax incidence involves not only "command," but also "the actual benefit for which the tax is paid." This case therefore does not support the legal theory for which it was cited.

In *Lucas* v. *Earl, supra,* this Court held that certain wages and fees *earned* by the *taxpayer* were taxable to him under Section 22(a), and that he could not escape the tax by *assigning* or *directing* that such income be paid directly to his wife. That case is of course not even in point because here the taxpayer did not earn the income, nor did he direct that it be paid to his wife or anybody else. Furthermore, it does not support the doctrine for which it was cited, because the taxpayer in that case *exercised* his *command* by "anticipatory arrangement," thereby *realizing* the *benefit* thereof. The Court declined to approve an arrangement "by which the fruits are attributed to a different tree from that on which they grew."

Helvering v. *Clifford, supra,* involved a *grantor* of a short term trust who *retained* and *reserved* to himself such control and dominion over the trust properties and income that this Court regarded him as *remaining* the *owner* thereof for purposes of taxation. Moreover, he *exercised* his *control* over the income by *directing* that it be paid to his wife, thereby *realizing* the *benefit* thereof. This Court said that Clifford, both grantor and trustee, "retained the substance of full enjoyment of all the rights which previously he had in the property." That case of course involved a plan of tax avoidance, "at best a temporary reallocation of income within an immediate family group," and is a far cry from the proposition for which it was cited.

In the *Horst* case this Court held that an *owner* of *property* may not escape tax on the income therefrom until he actually *divests* himself of the *source* of the *income.* There the taxpayer made a gift of interest coupons detached from bonds retained by him. While that case is not particularly in point, there is one very interesting paragraph in the opinion which shows how far afield the Fifth Circuit has gone in applying this case, as well as the cases above discussed. This Court, after citing a number of cases, including *Corliss* v. *Bowers, supra, Douglas* v. *Willcuts,* 296 U. S. 1, and *Helvering* v. *Clifford, supra,* said:

> "Underlying the reasoning in these cases is the thought that *income is 'realized'* by the *assignor* because he, who *owns* or *controls* the *source* of the income, also *controls* the *disposition* of that which he could have received himself and *diverts* the *payment* from *himself* to *others* as the means of *procuring* the *satisfaction* of his *wants.* The taxpayer has *equally enjoyed* the fruits of his labor or investment and obtained the *satisfaction* of his *desires* whether he *collects* and *uses* the income to procure those satisfactions, or whether he *disposes* of his *right* to *collect it* as the means of *procuring them.* Cf. *Burnet* v. *Wells,* 289 U. S. 670, 77 L. ed. 1439, 53 S. Ct. 761, *supra.*" (Italics ours.)

Later on in its opinion the Supreme Court, in referring to *Lucas* v. *Earl, supra,* which is also relied on by the Fifth Circuit, said:

> "The *exercise* of that power to procure the payment of income to another is the *enjoyment* and hence the *realization* of the income by him who *exercises* it." (Italics ours.)

The concept of income as defined by this Court in the above cases was again reiterated in a more recent and unanimous decision of the Court in *Harrison* v. *Schaffner,*

supra, which case is also cited and relied upon by the Fifth Circuit. In that case this Court held that an anticipatory assignment of trust income by way of gift does not preclude the taxation of such income to the beneficiary instead of the beneficiary's assignee. After discussing Section 22(a), 161 and 162 of the Act, the Court said:

> "In construing these and like provisions in other revenue acts we have uniformly held that they are not so much concerned with the refinements of title as with the actual command over the income which is taxed *and the actual benefit for which the tax is paid.* See *Corliss* v. *Bowers,* 281 U. S. 376, 74 L. ed. 916, 50 S. Ct. 336; *Lucas* v. *Earl,* 281 U. S. 111, 74 L. ed. 731, 50 S. Ct. 241, *supra*; *Helvering* v. *Horst,* 311 U. S. 112, *ante,* 75, 61 S. Ct. 144, 131 A.L.R. 655, *supra*; *Helvering* v. *Eubank,* 311 U. S. 122, *ante,* 81, 61 S. Ct. 149, *supra*; *Helvering* v. *Clifford,* 309 U. S. 331, 84 L. Ed. 788, 60 S. Ct. 554, *supra. It was for that reason that in each of those cases it was held that one vested with the right to receive income did not escape the tax by any kind of anticipatory arrangement, however skillfully devised, by which he procures payment of it to another, since, by the exercise of his power to command the income, he enjoys the benefit of the income on which the tax is laid.*" (Italics ours.)

Thus this Court again followed the same test laid down in the prior cases, namely, actual command plus *realization* or *enjoyment* of the income warrants the imposition of the tax. Therefore, it is apparent that the Fifth Circuit Court did not make an accurate statement of the law when it stated that "control over income warrants the imposition of the tax." By stating *only a part* of the rule, the Fifth Circuit has attempted to cut the heart out of those Supreme Court cases by eliminating the test of "realization" or "enjoyment" which test has been followed by this Honorable Court ever since Mr. Justice Holmes wrote *Corliss* v. *Bowers, supra.*

After making the statement quoted above, the Circuit Court closed its opinion with the following statement:

> "This principle is not to be limited in trust cases to situations where the grantor has retained controlling powers; the determinative consideration is the existence of actual dominion over the property whether it is retained or acquired. *Richardson* v. *Commissioner,* 121 F. (2) 1. Cf. *Commissioner* v. *Betts,* 123 F. (2) 534; *Jones* v. *Norris,* 122 F. (2) 6."

In the instant case petitioner was one of the trustees during the taxable years and acting in that capacity *managed* the trust properties. In that sense he *exercised* dominion over the properties, but surely a trustee is not made taxable by virtue of *managing* trust properties. During the taxable years petitioner did not *exercise* any *dominion* over the properties in an individual capacity for the simple reason that the properties were not "acquired" by him, as implied by the Court.

The *Richardson* case, *supra,* cited by the Circuit Court, does not stand for the rule for which it is cited, because in that case the taxpayer was regarded as the *grantor* of the trusts. The Commissioner determined in that case that Richardson was "in reality, the donor of the corpus of the five trusts and therefore, in substance, the grantor of those trusts, which were revocable by him." (See Board's Opinion, 42 B. T. A. 830 at 836.) The Second Circuit clearly indicated in that case that it did not regard the "gifts" made by Richardson to his wife as "genuine," and that it regarded him as real owner of the stock from the beginning to the end, and that he was the real grantor of the trust, even though his wife executed the instrument. The Second Circuit relied on *Richardson* v. *Commissioner,* 102 F. (2d) 697 (involving Richardson's brother), which decision was likewise predicated on the theory that the original "gift" by the husband to the wife was not "genuine," and that

the taxpayer had been the owner of the property all the time. See also *Richardson* v. *Commissioner,* 126 F. (2d) 562.

Moreover, the *Richardson* case obviously involved a scheme of tax avoidance, which distinguishes it from the instant case. There has never been the slightest implication, not even by the Commissioner, that the instant trust was created for tax avoidance or that it was anything other than a perfectly legitimate funded insurance trust. Judge Wallter of the Fifth Circuit stated in his dissenting opinion that:

> "There is not the slightest suggestion in this record that any saving of income taxes could possibly accrue to the taxpayer by the execution of the trust indenture.
>
> "There is not the remotest possibility of a tax saving to him to be accomplished by the trust agreement here under consideration." (See R. 76.)

In the *Betts* and *Jones* cases, which are the other two cases cited by the Fifth Circuit, the taxpayers were the *grantors* of the trusts and they *realized* the *benefit* of the *income* by *directing* the *manner* of its *disposition.*

Therefore, the three cases cited by the Circuit Court do not support the proposition that the rule is not to be limited to trust cases where the *grantor* has *retained* controlling powers, and that it makes no difference whether dominion over the property is "retained or acquired," because in all of those cases dominion was "retained" by the *grantors,* and moreover, that *dominion* was actually *exercised.*

From the foregoing it is apparent that the Fifth Circuit has attempted to broaden the concept of income as laid down by this Court, and it will hereinafter be shown that this new doctrine is unsound and its approval will result in serious consequences.

III

THE DECISION OF THE CIRCUIT COURT CONFLICTS WITH THE DECISION OF THE NINTH CIRCUIT IN COMMISSIONER v. GIANNINI, 129 F. (2d) 638, AND ALSO THE DECISION OF THE SIXTH CIRCUIT IN COMMISSIONER v. MOTT, 85 F. (2d) 315

The doctrine enunciated by the Circuit Court to the effect that "control over income warrants the imposition of the tax," whether the taxpayer takes it for himself or not, is in conflict with the decisions of the Ninth Circuit in the *Giannini* case. In that case, Giannini, President of the Bancitaly, was entitled to receive as compensation 5% of the yearly net profits, with a guaranteed minimum of $100,000.00. From January 1 to July 22, 1927, this percentage amounted to approximately $445,000 which was paid or credited to petitioner. The additional compensation for the balance of the year to which petitioner was entitled under the plan was approximately $1,500,000. However, petitioner refused to accept compensation for his services in addition to the $445,000. Upon his refusal, the board of directors decided to donate the $1,500,000 to the University of California for the establishment of the Giannini Foundation of Agricultural Economics. The Commissioner contended that petitioner was taxable on the compensation which he had refused. The Board of Tax Appeals, 42 B. T. A. 546, at 556, in rejecting that contention, said:

> "*It is elemental that an individual may refuse to enforce a right, forswear a debt due him, or relinquish a claim.* After such action it is equally basic that his debtor retains full possession and ownership of the thing renounced. It is obvious also that no one is compelled to accept compensation or payment for services or goods. *When he refuses to do so he cannot be charged with the amount so refused and abandoned, as an item of income. Under no theory of constructive receipt can it be compensation within the meaning and definition of income.*" (Italics ours.)

On appeal to the Ninth Circuit, the Commissioner advanced two arguments, which are set forth in the Court's opinion (page 640) as follows:

> "The Commissioner's argument in support of the claimed deficiency may be summarized as follows: That actual receipt of money or property is not always necessary to constitute taxable income; that it is the 'realization' of taxable income rather than actual receipt which gives rise to the tax; that a taxpayer 'realizes' income when he directs the disposition thereof in a manner so that it reaches the object of his bounty; . . .
>
> "Again it is stated by the Commissioner, 'Insofar as the question of taxation is concerned it would not seem to make much difference whether he directed Bancitaly Corporation to pay his compensation to the University of California or whether he merely told his employer to keep it.' "

The first argument above stated is, of course, a well-settled principle of law as laid down by the Supreme Court in the cases hereinabove discussed. The second contention, however, is substantially the same as the contention made by the respondent in the instant case. The Ninth Circuit stated the taxpayer's contention in the *Giannini* case as follows:

> "The taxpayer, on the other hand, urges that 'A person has the right to refuse property proffered to him, and if he does so, absolutely and unconditionally, his refusal amounts to a renunciation of the proffered property, which, legally, is an abandonment of right to the property without a transfer of such right to another. Property which is renounced (i. e., abandoned) cannot be "diverted" or "assigned" by the renouncer, and cannot be taxed upon the theory that it was received.' "

The Commissioner took issue with the taxpayer's argument and in support of his position cited some of the same

cases which have been cited by the Fifth Circuit in the instant case, including *Lucas* v. *Earl, supra, Helvering* v. *Horst, supra,* and *Harrison* v. *Shaffner, supra.* The Ninth Circuit distinguished those cases by showing that the taxpayers therein "realized" the "enjoyment" of the income by "procuring payment" to another or by "anticipatory assignment" to another. Then the Court stated as follows:

> "Now, turning again to the instant case. The findings of the Board, supported by the evidence, are to the effect that the taxpayer did not receive the money, *and that he did not direct its disposition.* All that he did was to unqualifiedly refuse to accept any further compensation for his services with the suggestion that the money be used for some worth-while purpose. *So far as the taxpayer was concerned, the corporation could have kept the money.* All arrangements with the University of California regarding the donation to the Foundation were made by the corporation, the taxpayer participating therein only as an officer of the corporation.
>
> "*In this circumstance we cannot say as a matter of law that the money was beneficially received by the taxpayer and therefore subject to the income tax provisions of the statute.* . . . In our opinion the inferences drawn by the Board are more reasonable and comport with that presumption of verity that every act of a citizen of good repute should be able to claim and receive." (Italics ours.)

The Government filed no petition for certiorari in the *Giannini* case. That decision conflicts, at least in principle, with the decision in the instant case.

The Circuit Court of Appeals for the Sixth Circuit has also decided that a person cannot be taxed on income which he did not actually or constructively receive. In *Commissioner* v. *Mott, supra,* the petitioner was trustee of three trusts under which he was entitled to receive 3% of the income as compensation for services. The petitioner, how-

ever, did not accept any compensation for his services as trustee, or receive any of the commissions to which he was entitled. The Commissioner held that he was nevertheless taxable thereon, since he could have received the commissions had he so elected. Both the Board and the Circuit Court, however, held that the amount of the commissions were not taxable income to the petitioner. The Sixth Circuit Court said, page 317:

> "We are in accord with the Board's view as to the error of the Commissioner in adding to the taxpayer's income 3 per cent. of the gross income of the trust estate. The taxpayer as trustee had the right as stated by the Board to render his services to the trust estate free of charge if he wished to do so. He did in fact render such services without charge. *To hold that he is chargeable with receiving compensation which he might have received but did not receive would be contrary, in our opinion, to the aims and purposes of the income tax laws.* Of course, there may be taxable income not actually received or reduced to possession, such as where it is credited to the account of or set apart for the taxpayer without limitation or restriction (Art. 51, Treasury Regulations 69); but in this case the evidence shows that no part of the 3 per cent. which the taxpayer might have charged was ever set apart for his benefit. He certainly never received any part of it. It is not claimed that deductions therefor were made from the gross income of the trust estates. *In our opinion there was no constructive receipt of it by the taxpayer which rendered it taxable to him.*" (Italics ours.)

In that case the taxpayer had "command" and "control" over the income. He could have taken it if he had elected to do so. Yet, the Sixth Circuit held that *he was not taxable thereon.* This decision certainly seems contrary to the rule laid down by the Fifth Circuit in the instant case which holds that petitioner is taxable on income

which he "controlled," and which he could have taken, but which he never elected to accept. Which of those decisions is correct? While this is a simple question, it is fundamental and important, and should promptly and definitely be settled by this Court.

IV

THE DECISION OF THE CIRCUIT COURT RAISES "UNCERTAINTIES IN THIS AREA OF FEDERAL TAX LAW," INTERSTATE TRANSIT LINES v. COMMISSIONER (UNITED STATES SUPREME COURT, No. 552, DECIDED JUNE 14, 1943), WILL RESULT IN ADMINISTRATIVE CONFUSION, AND WILL OPEN A TAX AVOIDANCE LOOP-HOLE NOT HERETOFORE AVAILABLE TO PERSONS IN HIGH SURTAX BRACKETS

Suppose H, a wealthy taxpayer in the high surtax brackets, irrevocably transfers securities to T, with directions to distribute currently $1,000.00 per year to his uncle and the remainder of the income to himself for life, with remainders over to his children. W, his wife, in lower surtax brackets, is given the right, upon five days' notice, to withdraw all the trust corpus or income for her own benefit, but she does not exercise that right.

Following the decision of the Fifth Circuit in the instant case, W, the wife, would be taxable on all the income for the reason that she was given the right to withdraw the trust corpus or income, irrespective of whether she "accepted" the offer and indicated her election to do so, and even though most of the income was "distributed currently" to H, the *grantor*.

Such a decision would doubtless make the Commissioner very unhappy because it would seem apparent that he could tax H under Section 162, and perhaps also under Section 22(a), because he *directed* the disposition of the income and actually *received* and *enjoyed* a portion there-

of. The Commissioner would in all probability petition this Court to upset such a decision, and frustrate the scheme of tax avoidance.

A slight change in the above facts will further demonstrate the erroneous conclusion reached by the Circuit Court. Suppose the same facts prevailed except that W, because of her absence from the country or for some other reason, was not advised of her powers during the taxable year, and, of course, gave no notice of her acceptance. Would the Court still hold that she was taxable on the income which was distributed during that year to H? Can H make W taxable on income without W's consent and acceptance, income which is received and enjoyed by H?

Surely the decision of the Circuit Court raises "uncertainties in this area of Federal tax law," and if the question is not definitely settled it will result in administrative confusion and multiple litigation.

In the instant case substantial portions of income were distributed to the grantor under the terms of a trust agreement and substantial sums were applied on the insurance premiums. Upon petitioner's death the corporate trustee was to collect the insurance proceeds, hold them in trust and pay the income to the *grantor* for life. Petitioner had no interest whatever in the insurance policies. He could not withdraw them without the grantor's consent and he could not make them payable to his estate. It must be apparent that amounts distributed currently under the grantor's direction and for her benefit were taxable to the *grantor* under Section 162 of the Act [perhaps also 22(a)]. She reported and paid the tax on amounts distributed currently to her and no one, not even the Commissioner, has ever denied that she owed the tax. Yet, the Commissioner, after the statute of limitations has run against the grantor, proposes to again tax that identical income against another person, the petitioner, under another section of the Reve-

nue Act, Section 22(a). In *U. S.* v. *Supplee-Biddle Hardware Co.,* 265 U. S. 189, this Honorable Court said that double taxation "is to be avoided unless required by the express words" of the statute. The Commissioner has never called the taxpayer's attention to those "express words," and, of course, there are none.

In *Estate of Gertrude Leon Royce et al.,* 46 B. T. A. 1090, the decedent had the right during her lifetime to withdraw any part or all of the trust corpus of a trust created by her husband. Upon her death, the Commissioner included the trust corpus in her estate for estate tax purposes under Section 302(a) of the Revenue Act. The Board, rejecting the Commissioner's determination, held that the right of the decedent to withdraw the trust corpus terminated upon her death, and that the trust corpus was not includable in her estate. The Commissioner acquiesced in that decision. I. R. B. No. 30, July 27, 1942.

In *Edith Evelyn Clark,* 47 B. T. A. 865, the taxpayer's husband created a trust and gave her the power to amend the trust in any way, including the right to withdraw any part or all of the corpus for her own benefit. The taxpayer relinquished said power, and the Commissioner held said relinquishment subject to the gift tax. The Board rejected the Commissioner's determination and held that no taxable gift had been made. The Commissioner acquiesced in that decision. I. R. B., December 21, 1942, No. 51.

It is believed that those two Board cases further demonstrate the unsoundness of the Circuit Court's decision in the instant case. By acquiescing in those cases, the Commissioner concedes that the trust corpus in the instant case would not be includable in petitioner's estate, and further that he did not have sufficient interest therein to make a taxable gift thereof. Yet, he contends, and the Circuit Court has held, that he is taxable on the income therefrom. It is not believed that such anomalous situations

could exist without unsound statutory construction. Everyone seems to concede that integration of the income, gift and estate tax laws is a desirable goal, but the decision of the Circuit Court in the instant case seems to be a step in the opposite direction.

V

CONCLUSION

By eliminating the essential elements of "realization" or "enjoyment" from the concept of income, the Circuit Court has enunciated a new doctrine much broader than the concept of income as defined by this Court. By applying this new doctrine to the present facts, the Court has concluded that income tax should be assessed against petitioner, even though the income was never received, assigned, realized or otherwise enjoyed by him. Apparently the Circuit Court would hold that the *grantor* of the trust (Amy Branch Jergens), the person who *directed* the *disposition* of the income and the person who *realized* the *enjoyment* thereof, should go tax free. (Otherwise there would be double taxation.) Petitioner does not believe that this new doctrine is a sound principle of law, but if it is, surely the uncertainties should be removed by a pronouncement of the Highest Court of the land.

For the foregoing reasons, it is respectfully submitted that this petition should be granted.

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APPENDIX

REVENUE ACTS OF 1936 AND 1938:

"**Sec. 22. Gross Income.**

(a) General Definition.—'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such Presidents and judges are hereby amended accordingly."

"**Sec. 161. Imposition of Tax.**

(a) Application of Tax.—The taxes imposed by this title upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct; . . ."

"**Sec. 162. Net Income.**

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * *

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year; . . ."

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556326—43

In the Supreme Court of the United States

October Term, 1943

No. 413

Andrew Jergens, petitioner

v.

Commissioner of Internal Revenue

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 26), now the Tax Court of the United States, is not officially reported. The opinion of the Circuit Court of Appeals for the Fifth Circuit (R. 71) is reported in 136 F. 2d 497.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 15, 1943 (R. 79), and petition for rehearing was denied on July 17, 1943 (R. 86). Petition for a writ of certiorari was filed October 7, 1943. Jurisdiction of the Court is in-

voked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer was given unlimited right, at any time, to terminate the trust created by his wife (with property which he had previously given her) and to take the income-producing corpus as his own. Due to his unfettered control of the property, is the income taxable to the taxpayer under Section 22 (a) of the Revenue Acts of 1936 and 1938?

STATUTES INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> *   *   *   *   *

This section appears without change in the Revenue Act of 1938, c. 289, 52 Stat. 447.

STATEMENT

The following facts were stipulated (R. 45–65) and found by the Board of Tax Appeals (R. 27–34):

The taxpayer is an individual residing in Palm Beach, Florida. The returns for the years involved were filed with the Collector of Internal Revenue for the Florida District at Jacksonville, Florida. (R. 27, 45.)

In 1922 the taxpayer caused to be transferred to his then wife 923 shares of the common stock of The Andrew Jergens Company of California (R. 27, 46).

In December of 1934 the taxpayer's wife applied for and received on December 26, 1934, insurance in the amount of $255,000 on the life of her husband (R. 27–28, 46). By the terms of the policies the wife was designated as the owner, beneficiary, and the one obligated to pay the premiums (R. 27–28, 46). On December 31, 1934, the taxpayer's wife created a trust, naming The First National Bank of Cincinnati, Ohio, and her husband as co-trustees (R. 28, 46).

On the same day the taxpayer's wife, pursuant to the trust agreement, transferred to the trust all her right, title, and interest in the insurance policies and 685 shares of the Jergens stock above referred to (R. 28, 46–47).

Under the terms of the trust, the net income was to be applied (a) to pay the premiums on the

life-insurance policies issued on the life of the taxpayer and held in the trust; (b) to make certain monthly payments to an aunt of the wife; (c) to pay the remaining net income to the wife during her life (R. 32, 54–55).

The trust instrument provided that the co-trustee bank should follow and abide by the instructions of the taxpayer, so long as he lived, "in all matters pertaining to the Trust property" (R. 31, 53). The taxpayer was vested with the sole right to vote the stock held in the trust and to designate the investment counsel whose instructions the bank was to follow (R. 31, 53).

The trust instrument also provided the following:

(1) That during the life of the grantor, the taxpayer should have full authority to withdraw any part or all of the corpus of the trust, with the exception of the policies of insurance upon his own life (which could only be withdrawn with the consent of the grantor) (R. 32, 55);

(2) that unless the trust was terminated and revoked by the taxpayer, prior to the death of the grantor, the trust should be irrevocable (R. 33, 55);

(3) that the taxpayer, in addition to the power to terminate or revoke the trust, should also have the power to alter, modify or amend the agreement in any respect whatsoever (except that he could not make the proceeds of the insurance policies payable to his estate) (R. 33, 55–56);

(4) that in the event the taxpayer had not terminated or revoked the trust prior to the death of the grantor, the trust should terminate at her death and all of the trust property be then transferred to the taxpayer if he be living or to the lawful issue or any legally adopted children of the taxpayer and the grantor (R. 33, 56);

(5) that in the event the taxpayer should predecease the grantor, leaving no issue or adopted children, the trust property should continue in trust for a period of five years after the grantor's death, as a charitable and educational trust, the terms of which are not here relevant (R. 33, 56–57).

During 1936, 1937, and 1938, the taxable years in question, the trust agreement was in full force and effect (R. 28, 47). For these years the trustees filed fiduciary income tax returns for the trust and paid tax on the trust income, and the taxpayer's wife reported as income the sums received by her from the trust and paid tax thereon (R. 29, 48).

Deficiencies were assessed by the Commissioner against the grantor of the trust on the theory that the trust income was entirely taxable to her (R. 30, 48–49). The Board of Tax Appeals held that the income was not taxable to the grantor and the Fifth Circuit Court of Appeals affirmed the Board in *Commissioner* v. *Jergens,* 127 F. 2d 973.

Deficiency assessments against the taxpayer of \$6,060.50 for 1936, \$15,268.93 for 1937, and

$13,048.23 for 1938, on the ground that the income was taxable to him were, however, sustained by the Board (R. 35) and affirmed by the Fifth Circuit Court of Appeals (R. 79).

ARGUMENT

The decision of the court below is in accord with that of the Circuit Court of Appeals for the Second Circuit upon substantially identical facts in *Richardson* v. *Commissioner,* 121 F. 2d 1, certiorari denied, 314 U. S. 684, rehearing denied, 314 U. S. 714. This Court has clearly enunciated the principles followed by the Board of Tax Appeals and the court below in determining that the taxpayer's unfettered control over the trust property was the equivalent of ownership for tax purposes and that the trust income was taxable to him under Section 22 (a) of the Revenue Acts of 1936 and 1938, *supra. Harrison* v. *Schaffner,* 312 U. S. 579; *Helvering* v. *Horst,* 311 U. S. 112; *Helvering* v. *Clifford,* 309 U. S. 331; *Lucas* v. *Earl,* 281 U. S. 111; *Corliss* v. *Bowers,* 281 U. S. 376.

The taxpayer had the power to alter, modify and amend the trust, except that he could not make the proceeds of the insurance policies payable to his estate. Since all of the income here involved was produced by other property than the insurance policies, any limitation of his power to deal with them is of no consequence. The taxpayer also had the absolute power to withdraw

any or all of the income-producing property of the trust and to devote it to his own use or benefit. His power over and control of the property was far greater and more immediate than that of the taxpayer in *Helvering* v. *Clifford, supra.* Taxpayer relies on two distinctions:

(1) That he was not the grantor of the trust, and

(2) that he did not actually take the property from the trust. Both distinctions are without substance. The fact that he actually had complete dominion over the property, whether it was acquired or retained, is the vital factor. *Richardson* v. *Commissioner, supra.* Because of taxpayer's full authority to rewrite the trust and dispose of the income and corpus as he pleased, he bore the same relationship to the property as a grantor. Nor is it material that he did not choose to terminate the trust. He was entirely free to do so. The principle to be followed was expressed by this Court in *Corliss* v. *Bowers, supra* (p. 378):

> The income that is subject to a man's unfettered command and that he is free to enjoy at his own option may be taxed to him as his income, whether he sees fit to enjoy it or not. * * *

The decision of the lower court is not in conflict with *Commissioner* v. *Giannini,* 129 F. 2d 638 (C. C. A. 9th), or with *Commissioner* v. *Mott,* 85 F. 2d 315 (C. C. A. 6th), as alleged by the taxpayer. In each of those cases the taxpayer

unconditionally declined to accept compensation for services rendered and in each instance it was held that the taxpayer was not taxable upon the income which he had refused to accept. In neither instance did the taxpayer accept any control over the disposition of the income. In the present case, the taxpayer was irrevocably given a power of revocation of the trust which he accepted. From then on he had complete command of the source of the income. He also accepted unlimited power to alter or amend the provisions of the trust relative to the income therefrom. Although the foregoing decisions may be doubtful they are not in conflict with the decision herein.

CONCLUSION

The decision of the court below is correct. There is no conflict. The petition should be denied.

Respectfully submitted.

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